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U. S. No. 132

IN THE

Supreme Court of the United States

October Term, 1965

MARGARET L. HOLT and KATHLEEN L. McMAHON, individually and on behalf of all other shareholders of Alleghany Corporation similiarly situated,

Petitioners,

AGAINST

ALLAN P. KIRBY, CHARLES T. IRELAND, JR., FRED M. KIRBY and ALLEGHANY CORPORATION,

Respondents

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit—Granted June 1, 1965.

BRIEF OF *AMICUS CURIAE* ON ISSUE OF "EXCLUSIVE JURISDICTION"

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BRIEF OF *AMICUS CURIAE* ON ISSUE OF "EXCLUSIVE JURISDICTION"

The Interest of *Amicus Curiae*

The common stockholders of Alleghany Corporation, except for this brief, have no representation on the jurisdictional issue. Although it was presented as Question 5 in the petition for the writ, petitioners abandoned the question after the writ was granted.*

* The mistaken reasons for their abandonment are set forth in Application for leave to file brief as *amicus curiae*, page 4.

Randolph Phillips, *amicus curiae* herein, has been a holder of 100 shares of the common stock of Alleghany Corporation since November, 1954. His group negotiated the $3,000,000 cash settlement, plus return of control of the $3 billion Investors Diversified Services, Inc. system of investment companies, that constituted the total settlement of which only Kirby's share is at issue herein. He acted as the representative of the common stockholders group opposing the initial settlement of $700,000 cash negotiated by attorney Abraham L. Pomerantz (R. 2308-2309; 218 F. Supp. at 177).

Because of this role and because without the brief herein the common shareholders will be deprived of representation in this Court on the jurisdictional issue, *amicus curiae* has a double interest in this case. In addition, he and his group were the initial victims of the fraudulent suppression of documents alleged herein. Accordingly he supports the position of petitioners and believes that the issue briefed herein should be determinative of the result.

The Facts

The Findings of the Court below on the "exclusive jurisdiction" issue.

The *Per Curiam* decision of the Court below on this issue was set forth in the following note 1:

> "In its reply brief on rehearing in banc appellant (Alleghany Corporation) points out for the first time that since the claim in the state court suit relating to the exchange of stock was grounded in part on an allegedly false and misleading proxy statement, see §14(a) of the Securities Exchange Act of 1934, 15 U. S. C. §78n(a) and SEC Rule

X-14A-9, federal jurisdiction existed, see J. I. Case Co. v. Borak, 377 U. S. 426 (1964), and argues that §27 of the 1934 Act, 15 U. S. C. §78aa, made such jurisdiction exclusive and rendered the state judgment void. We find it unnecessary to rule on the argument. For, apart from any other factors, the issue of jurisdiction was raised in *and decided by the New York courts,* 1 App. Div. 2d 662, 146 N. Y. S. 2d 213 (1955), motions for reargument and for leave to appeal to the Court of Appeals denied, 1 App. Div. 2d 773, 149 N. Y. S. 2d 213 (1956); and no attempt to secure review by the Supreme Court of the United States was made. See Treinies v. Sunshine Mining Co., 308 U. S. 66, 78 (1939). On this the court is unanimous'' (R. 2375-2376) (340 F. 2d 311). (Emphasis supplied.)

The litigation cited by the court below was with respect to the $700,000 cash settlement negotiated in the New York State Supreme Court in 1955, approval of which the federal court enjoined from being pleaded res judicata because of the ''unconscionable conduct'' of attorney Pomerantz and the Young, Kirby, Murchison defendants ''in attempting to bind their adversaries (in the federal court) by a settlement to which they were not parties.''

In August 1955 the shareholders of Alleghany received a notice that attorney Abraham L. Pomerantz had negotiated with the defendants in *Zenn et al.* v. *Anzalone et al.* a settlement in the New York State Supreme Court of $700,000 cash for all the claims asserted therein against defendants Robert R. Young, Allan P. Kirby, Murchison Brothers and others (R. 729-747). The stipulation of settlement recited that Kirby ''has neither appeared nor an-

swered in this action" (R. 729). It was signed by David W. Wallace as Kirby's "attorney in fact" (R. 736).

In October 1955 the plaintiffs in *Breswick & Co.* v. *Briggs et al.*, in the federal court obtained an injunction against the *Zenn* defendants which prohibited them pleading any judgment based on the State Court settlement as *res judicata* of the *Breswick* claims in the federal court (135 F. Supp. 397, 406):

> "Four days after the three-judge court in Breswick & Co. v. United States, supra, granted a preliminary injunction and expressed conclusions of law substantially helpful to plaintiffs' claim that Alleghany was subject to the Investment Company Act, defendants and counsel (Pomerantz) for another group of stockholders announced a stipulation of settlement to terminate the present action as well as all other derivative actions based upon the same alleged misconduct of the directors * * *.
>
> Plaintiffs can be protected by enjoining defendants from using as a defense in this action, any judgment which may be entered upon a stipulation of settlement not negotiated with the present plaintiffs or their representatives. In this way there is no interference in the State Court proceedings nor is any doubt cast upon its judgment, *but these defendants are precluded from taking inequitable advantage of their unconscionable conduct in attempting to bind their adversaries by a settlement to which they were not parties.*" (Emphasis supplied.)

Speaking explicitly of attorney Abraham L. Pomerantz, the Court stated:

> "Plaintiffs in the other derivative actions and the defendants ask that the lawyer designated as

> general counsel in those actions be designated as general counsel for the proposed consolidated action. * * * *To place this action under his control seems hardly fair to plaintiffs, particularly after he has already committed himself to a settlement based in part upon an incomplete evaluation of their efforts.*" (Emphasis supplied.)

Objectant stockholder Rosen's unsuccessful attempt in 1955 to obtain from the State Court a ruling on the issue of "exclusive jurisdiction" with respect to the federally enjoined $700,000 Pomerantz settlement.

After the federal court decision an Alleghany shareholder who appeared in the State Court as an objectant to the $700,000 Pomerantz settlement (Samuel R. Rosen) moved in New York Supreme Court to enjoin any further proceedings before the Referee on 2 grounds: (i) the settlement had been unfairly negotiated as shown by the above cited federal court decision, and (ii) the district courts of the United States had "exclusive jurisdiction" over the claim set forth in the first count of the *Zenn* state court complaint alleging that the 1950 IDS transaction violated Section 14(a) of the Securities Exchange Act of 1934 and the rules and regulations thereunder.

Mr. Justice McGivern (who had appointed the Referee) denied the motion *without opinion* and Rosen appealed. On the appeal the Appellate Division's *entire* opinion was as follows:

> "We construe the order of reference, in entitling appellant to raise any question as to the fairness, reasonableness or adequacy of the settlement, to include the issue and the effect, if any, of the exclusion of persons from the negotiations for settle-

ment. We assume that unless there is an adverse effect on the settlement by reason of such exclusion, exclusion will not have been shown to be improper."

Zenn v. *Anzalone*, 1 App. Div. 2d 662, 146 N. Y. S. 2d 213 (1955).

Thereupon Rosen moved for leave to reargue or, in the alternative, to appeal to the Court of Appeals, stating "Appellant now seeks reargument only on that issue, the question of jurisdiction of the subject matter". The Appellate Division denied the motion for reargument; it also denied leave to appeal to the Court of Appeals. *Zenn* v. *Anzalone*, 1 App. Div. 2d 773, 149 N. Y. S. 2d 213 (Jan. 31, 1956).

This is the entire court record on which the court below decided that the jurisdictional issue was *res judicata.*

The appellate decision of the State Court upon which the Court below relied for its finding of res judicata shows that the Appellate Division never reached the issue of "exclusive jurisdiction" in the federal court or arguendo at the most decided it sub silentio.* Kirby misled the Court below by failing to provide for the record a copy of defendants' brief in the Appellate Division showing that they successfully urged that consideration of the jurisdictional issue was "premature".

There were 8 causes of action alleged in the *Zenn* complaint (R. 701, 723). The "exclusive jurisdiction" issue arose only with respect to the first one (R. 704-705). At

* We doubt that a court as responsible as the Appellate Division may reasonably be found to have "decided" so important a point *sub silentio.*

the most the above-quoted Appellate Division decision relied on by the Court below indicates that the issue—despite its importance—*might* have been "decided" to quote the operative verb of the *Per Curiam* decision of the court below—*sub silentio*. It seems clear however that it did not reach the issue. Defendants' attorney Thomas F. Daly in the "Brief for Defendants-Respondents Young, et al." filed in the Appellate Division—First Department, in *Zenn* v. *Anzalone*, New York County Clerk's Index No. 7244/1954, stated:

> "3. We submit that for all the reasons stated in this and the preceding point of this brief, appellant's attack upon the jurisdiction of the Court below is unfounded. We add, however, the final observation that appellant's attack on the proceedings below *is in any event premature.*
>
> Alleghany has applied to the Court below for an inquiry into and the approval of the proposed settlement. *The Court below has, so far, neither granted nor denied the application.* What it did do was to appoint a Referee in order to assemble and report on all relevant facts and considerations bearing upon the requested approval of the settlement. Among the matters thus to be considered by the Referee and by the Court below are the extent to which the Court has power to approve the settlement. If the Referee or the Court below should conclude that any part of the proposed settlement cannot be passed upon by the state court, they will doubtless so advise the parties and notify them either to limit their settlement or to eliminate from the complaint the reference therein to the Exchange Act. If such a suggestion should be made and if it should be adopted by the parties,

the issue presented by appellant would become moot. We submit, therefore, that appellant's present jurisdictional attack is premature and that this Court should defer consideration thereof until such time as a judgment of the Court below approving the proposed settlement may be presented to this Court for review" (pp. 15-16). (Emphasis supplied.)

The enjoined 1955 settlement of attorney Pomerantz of $700,000 became moot as a result of the $3,000,000 cash settlement obtained by the Breswick plaintiffs in December, 1959.

The record shows that in 1958 in an effort to vacate the federal court injunction the Breswick defendants, including Kirby who was served and had appeared in the federal court action—unlike the State Court action—offered to settle the claims against them for $1,000,000 cash and the Murchisons offered to return to Alleghany control of the $3 billion Investors Diversified Services, Inc. system of investment companies (R. 2299). This offer was rejected by the Breswick plaintiffs as inadequate (R. 2301). Nevertheless the Referee whose appointment attorney Pomerantz and the defendants had obtained in the State Court (R. 741) proceeded to issue his report dated November 18, 1958 approving the new settlement as "fair, reasonable and adequate" (R. 2299-2300). A motion to confirm was made before Mr. Justice McGivern in the New York State Supreme Court. An opinion approving the settlement as "fair and reasonable" and terming the Referee's Report "a lucid, painstaking and comprehensive" report was filed by Mr. Justice McGivern on March 9, 1959 (R. 1717, 1719, 1720). In federal court, however, Judge Dimock refused to accept the report as a basis for vacating the

injunction because the Breswick plaintiffs in hearings before the same Referee as Special Master in the federal court had not been given an opportunity to present their evidence, including the testimony of Kirby (R. 862, 873-874).

Finally, in December, 1959 Kirby offered to settle the Breswick-Zenn claims against him for $1,100,000; Young for $900,000 and the Murchison-Richardson group for $1,000,000, or a total of $3,000,000 cash plus the return of the controlling stock in IDS (R. 2339). This was $2,000,000 more than Justice McGivern and Referee Fitzsimmons had found "fair and reasonable", and $2,300,000 more cash than had been obtained by attorney Pomerantz, as well as the IDS stock. In fact, Judge Friendly found that Pomerantz "the stockholders general counsel" (R. 2368) had opposed the efforts of *amicus curiae's* group represented by attorney Seymour L. Graubard to obtain the increased settlement (R. 2368).

Summary of Argument

The New York State Supreme Court did not have jurisdiction to enter the judgment dismissing and releasing the claim of the Alleghany shareholders against Allan P. Kirby, based on the alleged violation of the Securities Exchange Act of 1934, since "exclusive jurisdiction" over alleged violations of the Act and the rules and regulations thereunder is vested "in the district courts of the United States" (Section 27). Inasmuch as the State Court complaint explicitly pleaded facts (not pleaded to support a common law claim) as a violation of the federal statute, there is no substance to defendant's contention that the federal claim is mere "surplusage". *J. I. Case* v. *Borak*, 377 U. S. 426 (1964). To uphold this contention would be to violate the "long-established principle" that "the party who brings a suit is master to decide what law he will rely upon." *The Fair* v. *Kohler Die & Specialty Co.*, 228 U. S. 22, 25.

The Court below did not reach this issue. It was misled by Kirby to believe that it was *res judicata* because it had been "decided" by the New York State Courts. Examination of the defendants' brief in that court shows the Appellate Division had been urged that the issue was "premature". Since the decision cited by the court below makes no reference to the jurisdictional issue, the success of the argument of "prematurity" seems obvious and the issue was never in fact "decided" by the State Court. Kirby has no standing to claim the issue *res judicata* as to himself. It was "raised" by an objecting stockholder, not a party plaintiff, on a motion in a case in which Kirby did not appear as a party defendant and in relation to the enjoined $70[illegible] settlement that became moot. In addition, Kirby [illegible]ed his excusal from testifying in the State Court on the ground of medical testimony that he had "a dangerous heart condition" although subsequently he testified in other proceedings without medical objection and without informing the State Court Judge prior to entry of the final judgment herein.

ARGUMENT

POINT ONE

The New York State Court had no jurisdiction to enter its judgment authorizing settlement and release of the federal claim against Kirby based on the violation of the Securities Exchange Act of 1934, since "exclusive jurisdiction" over such violations is vested "in the District Courts of the United States".

The federal claim alleged in the Zenn State Court amended complaint.

The State Court plaintiffs in *Zenn et al.* v. *Anzalone et al.*, alleged in their First Cause of Action 2 distinct claims:

> (1) For rescission of the 1950 Exchange Transaction on the ground that the consideration therefor was inadequate by the sum of $148,273.79, or for an accounting by individual defendants for that sum [Pl. Ex. 1, ¶¶ 11(c), 13(a)] (R. 704).
>
> (2) For rescission of that transaction on the ground that the proxy material was false and misleading under Section 14(a) of the Securities Exchange Act of 1934, 15 U. S. C. §78n(a), and Rule X-14A-9, thus voiding the proxies procured thereby and the resulting resolution of Alleghany's Stockholders authorizing the exchange. [Pl. Ex. 1, ¶¶13(b), 14, 15] (R. 704-705). *Id.* §29, 15 U. S. C. §78cc.

Contrary to the contention of Kirby below, the *Zenn* plaintiffs did not plead a common law right in either the *Zenn* (State) or the duplicate *Zenn* (Federal) complaint with respect to the proxy solicitation.* Instead, they ex-

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* *Zenn et al.* v. *J. J. Anzalone, Allan P. Kirby et al.*, USDC, SDNY, Civil Action No. 92-205 (R. 2332, footnote). This action is still pending.

plicitly pleaded a violation of Section 14(a) of the Exchange Act and Rule X-14A-9 of Regulation X-14 in the precise words of the statute:

> "(b) The aforesaid exchange transactions should also be rescinded for the additional reasons set forth in paragraphs '14' and '15'.
>
> "14. The notice of annual meeting and proxy statement of April 6, 1950 (as supplemented by a further statement mailed by Alleghany to its stockholders on or about April 26, 1950), to the knowledge of the individual defendants, contained statements which, at the time and in the light of the circumstances under which they were made, were false and misleading with respect to material facts and omitted to state material facts necessary to make the statements therein not false or misleading, as follows:" *
>
> * * * * *
>
> "15. (a) The proxy statement, notice of meeting and supplementary letter of April 26, 1950, violated §14(a) of the Securities Exchange Act of 1934 and Rule X-14A-9 of the Securities and Exchange Commission." (Emphasis supplied) (R. 704-705).

Federal jurisdiction is "exclusive" over an alleged violation of the S. E. C. proxy regulation and rules promulgated under Section 14(a) of the Securities Exchange Act of 1934.

While the state court clearly had jurisdiction to dispose of the first claim of failure to pay the agreed considera-

* The underlined language is almost an exact repetition of the prohibitory language in S.E.C. Proxy Rule X-14A-9 (17 C.F.R. §240.14a-9).

tion, based on local law, it had no jurisdiction to direct dismissal, settlement or release of the federally based claim. Under section 27 of the Act, 15 U. S. C. §78aa:

> "The district courts of the United States . . . shall have *exclusive* jurisdiction of violations of this chapter *or the rules and regulations thereunder*, and of *any and all* suits in equity and actions at law brought to enforce any liability or duty created by this chapter *or the rules and regulations thereunder.*" (Emphasis supplied.)

A shareholder claim, asserted derivatively or directly, for relief from a consummated corporate transaction effected by violation of section 14(a) of the Act or any regulation or rule, such as Rule X-14A-9, thereunder is one within the exclusive jurisdiction of the federal court. *J. I. Case Co.* v. *Borak*, 377 U. S. 426, 433-35, 428, n. 2 (1964). The state courts have not taken jurisdiction to consider similar statutory claims in any context—for judgment, settlement or otherwise—even if coupled with clearly pleaded state law claims. See *American Distilling Co.* v. *Brown*, 295 N. Y. 36 (1945); *Mekrut* v. *Gould*, 16 Misc. 2d 326, 188 N. Y. S. 2d 6, 9 (Sup. Ct. N. Y. Co. 1959); *Standard Power & Light Corp.* v. *Investment Assoc.*, 51 A. 2d 572, 579 (Del. 1947).

This Court in J. I. Case v. Borak, 377 U. S. 426, declared that the "concurrent federal-state tort theory" is not valid.

Prior to the recent decision of this Court in *Borak,* a stockholder, suing derivatively, was precluded in two circuits from asserting a claim for violation of section 14(a) of the Securities Exchange Act of 1934. *Dann* v. *Studebaker Packard Corp.,* 288 F. 2d 201 (6th Cir. 1961); *Howard* v. *Furst,* 238 F. 2d 790 (2d Cir. 1956), cert. den. 353 U. S. 937 (1957). In addition to the finding of these courts that proxy rules relate only to each individual's corporate franchise and thus give rise to only a representative right of action, the courts justified their position by reference to the nature of a section 14(a) violation relative to the wrong done the corporation. Thus, the court in *Howard* v. *Furst, supra,* 238 F. 2d, at 793-94, refused jurisdiction of a derivative claim for rescission of a corporate transaction based on violation of section 14(a), on the ground, *inter alia,* that every essential element of the charged derivative wrong depended upon state law, without regard to the proxy violation, and hence the latter issue was "a mere excrescence or superfluity". The *Dann* court similarly denied a right to such relief as a matter of federal right, and held that plaintiff's claim was one arising under state law (288 F. 2d, at 214).

But in *Borak* this Court corrected the law as construed in *Dann and Howard* v. *Furst.* As to *Dann,* the Court said (377 U. S., at 434):

> "[I]n *Dann* v. *Studebaker-Packard Corp.,* 288 2d 201, * * * it was held that the 'preponderance of questions of state law which would have to be interpreted and applied in order to grant the relief

> sought . . . is so great that the federal question involved . . . is really negligible in comparison.' "

This Court then stated with respect to a derivative right of action under Section 14(a) which also involved a proxy solicitation and a stockholder vote:

> "But we believe that *the overriding federal law applicable here would,* where the facts required, *control the appropriateness of redress* despite the provisions of state corporation law, *for it 'is not uncommon for federal courts to fashion federal law where federal rights are concerned.' Textile Workers* v. *Lincoln Mills,* 353 U. S. 448, 457 (1957). *In addition, the fact that questions of state law must be decided does not change the character of the right; it remains federal."* (Emphasis supplied.)*

Thus the derivative claim based upon violations of Section 14(a) of the Securities Exchange Act of 1934 [as pleaded in *Zenn* (State)] is peculiarly a matter of federal right, even though the allegations upon which the claim is based might also make out a claim under state law. Under section 27 of the Act, this federal right is one determinable *only* by the federal district court, the exclusive forum, because it involves "violations of * * * the rules (Rule X-14-9) and regulations (Regulation X-14) thereunder (Section 14a)".

* In the claim at issue herein, unlike in *Borak, supra,* there are no questions of state law that "must be decided." *Borak* involved a merger, a question peculiarily governed by state statute.

Neither the law of the State of Maryland where Alleghany is incorporated nor the common law imposes any duty, as does Regulation X-14 of the Securities Exchange Act of 1934, to pre-file proxy statements with the S. E. C. and to solicit stockholder approval of resolutions at annual meetings only pursuant to proxy statements that conform to S. E. C. imposed standards of truth and full disclosure as defined by that agency and the federal courts under the statute.

The above considerations make clear that not to pre-file a truthful proxy statement and the circulation of a proxy statement that does not meet the statutorily-imposed standards as defined by the S. E. C. of truth and full disclosure are violations of a peculiar federal "duty or liability created" by the Securities Exchange Act of 1934 (Sec. 27).*

Kirby's argument, if upheld, would nullify the rule that "the party who brings a suit is master to decide what law he will rely upon." The Fair v. Kohler Die & Specialty Co., 228 U. S. 22, 25; Pan American Petroleum Corp. v. Superior Court, 336 U. S. 656, 662.

In the Court below Kirby argued that "Where a given set of facts creates a right to relief in the state courts under state law as well as in the federal courts under a

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* Kirby told the Court below that the explicit reliance on Section 14(a) in the *Zenn* State complaint was a mere "excrescence". But, that was the view of *Dann* v. *Studebaker Packard Corp.*, 288 F. 2d 201 (6th Cir. 1961) and *Howard* v. *Furst*, 238 F. 2d 790 (2d Cir.), *cert. den.* 353 U. S. 937 (1957) which were overruled by this Court in *Borak*.

statute, the mere fact that the federal court has exclusive jurisdiction over cases brought under the federal statute does not operate to divest the state courts of jurisdiction to grant relief on the same facts under state law." The fallacy in this argument applied to the issues here is that "the same facts" were not pleaded to secure relief under state law—namely the facts of proxy violation and statements that violated the standards of Rule X-14A-9. They were exclusively pleaded under the claim based on violation of the federal statute. As this Court stated in *Pan American P. Corp.* v. *Superior Court*, 366 U. S. 656, 662 (1961), this Court stated:

> "But questions of exclusive federal jurisdiction and ouster of jurisdiction of state courts are, under existing jurisdictional legislation, not determined by ultimate substantive issues of federal law. The answers depend on the particular claims a suitor makes in a state court—*on how he casts his action.*" * (Emphasis supplied.)

The law in New York is that where a federally created right is pleaded, a state court cannot comb the pleading for facts in order to fashion a common law claim for the purpose of sustaining its jurisdiction. *Levine* v. *Silverman*, 43 Misc. 2d 415, 417, 251 N. Y. S. 2d 68 (Sup. Ct. Monroe Co. 1964); *Malkan* v. *General Transistor Corp.*, 207 N. Y. S. 2d 345, 347-48 (Sup. Ct. Queens Co. 1960). We submit the rule is applicable here.

In *Levine*, plaintiffs pleaded, *inter alia*, a claim based upon Section 10 of the Exchange Act. That section makes

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* *Pan American* did not deal with a federal claim pleaded in a complaint. In giving effect to a state court determination in each of the cases relied upon below by Kirby this Court explicitly relied upon the express assertion of a common law claim for relief unmixed with a federal right.

it unlawful to use any instrument in interstate commerce to deceive another in effectuating a sale of securities. The facts giving rise to that statutory claim (like the facts here giving rise to a Section 14(a) claim) conceivably could support a common law claim of fraud, if pleaded as such. Upon a motion to dismiss, however, the New York Supreme Court held that under Section 27 of the Exchange Act a state court had no jurisdiction over a claim so pleaded. If an option to plead a federal or a common law claim was available to the *Zenn* plaintiffs, the option, like the one in *Levine*, was exercised in favor of the assertion of a federal claim. Thus, the *Zenn* (State) court, like the *Levine* court, did not have jurisdiction to hear, determine or settle the explicitly pleaded federal claim.

POINT TWO

The Court below erroneously assumed that "the issue of jurisdiction was * * * decided by the New York courts".

In its *per curiam* decision filed January 12, 1965, the Court below in note 1 erroneously assumed "the issue of jurisdiction was * * * decided by the New York courts". The Court cited in support thereof *Zenn* v. *Anzalone*, 1 App. Div. 2d 662, 146 N. Y. S. 2d 213 (1955), motions for reargument and for leave to appeal to the Court of Appeals denied, 1 App. Div. 2d 773, 149 N. Y. S. 2d 213 (1956) (R. 2375-2376).

As we have shown (this brief, pp. 4-7, *supra*) the issue of jurisdiction was "raised," but it was not "decided."

POINT THREE

Since Kirby misled the court below by not disclosing the brief of defendants in the Appellate Division in which they successfully urged that consideration of the issue of "exclusive jurisdiction" was "premature", he was not entitled to the finding of *res judicata*.

The facts on this point are set forth at pp. 4-7, *supra*. Accordingly, Kirby is not entitled to plead that the issue of "exclusive jurisdiction" is *res judicata* as to him.

POINT FOUR

The record cited by the court below is insufficient to support the conclusion that Kirby is entitled to be sustained on the defense of *res judicata* on the issue of "exclusive jurisdiction".

The record is insufficient for a number of reasons to sustain this defense:

(i) the decisional record relied upon by the Court below shows no reference to the issue of "exclusive jurisdiction".

(ii) the brief for defendants in the Appellate Division, New York State Supreme Court—First Dept.—shows that their attorney Thomas F. Daly urged upon the Court in point 3 at pp. 15-16 thereof that it was "premature" to decide the jurisdictional issue (pp. 4-7, *supra*). Since the Appellate Division made no reference to the jurisdictional issue in its one-paragraph decision (pp. 5-6, *supra*), it is reasonable to assume the latter was persuaded not to determine it because of this argument of "prematurity". This is more reasonable than the

assumption that a court as responsible as the Appellate Division would decide so important an issue as the jurisdiction of the federal courts *sub silentio*.

(iii) Kirby was not a party nor had he appeared in the State Court at the time of the decisions cited by the court below nor did he become a party in December 1959 at the time of the order approving the settlement (R. 2340). In fact his attorney informed the State Court in December, 1959 that he was not appearing, and that he was merely in court to present the stipulation of settlement (R. 2112).

(iv) Objectant Rosen who raised the jurisdictional issue in the State Court in 1955 was not a party plaintiff nor does the record show that he at any time pleaded he was acting as a class representative.

(v) The 1955 offer of settlement in the amount of $700,000 cash—in opposition to which Rosen appeared as an objectant—was enjoined and became moot (pp. 4, 5, 8, *supra*).

(vi) Kirby obtained a ruling by the State Court Referee that he was excused from testifying because his life "would be endangered" if he did (R. 1569, note, 2087-2088). Thereafter he testified for 2 days in this action (R. 421-481) for 3 days in another action in March, 1960,* and for 2 days before the S. E. C. in March, 1963,** on none of which occasions did he claim that giving his testimony would endanger his life.

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* *Schwarz* v. *Bowman*, USDC, SDNY, Civil Action 116-303, Record on Appeal.

** *In the Matter of Investors Mutual, Inc.*, File No. 812-1550, R. 4450 *et seq.* (1963).

(vii) The Referee who excused Kirby was paid by Alleghany Corporation under Kirby's control a fee of $125,000, without appeal of the court order awarding it.*

Judge Leonard P. Moore for the majority stated with respect to the transaction "whitewashed" by the Referee:

> "Alleghany's real dissatisfaction must be based upon the Referee's and Supreme Court's decisions. There was certainly enough evidence presented to justify a rejection of the proposed settlement" (R. 2343).

We suggest that the fact that the Referee's fee is paid by the Corporation under defendant's control, which corporation if it objects thereto or appeals an award can diminish the amount, produces an unwholesome situation which under *Hansberry* v. *Lee,* 311 U. S. 32, 40-46 and the other facts herein disentitles Kirby to plead *res judicata.* Does "the procedure adopted fairly insure the protection of the interests of absent parties who are to be bound by it"? (311 U. S. at 42). As Judge Friendly stated: "All the dynamics conduce to judicial approval of such settlements" (R. 2368) in the New York State Supreme Court. It should be noted that Judge Moore commented that attorney Pomerantz was the "most skilled and experienced" in such settlements (R. 2331). The Referee, whose existence as such is made possible by the Pomerantz settlement, received his $125,000 fee and Pomerantz a fee of $350,000 for his $700,000 cash settlement. *Zenn* v. *Anzalone,* N. Y. L. J., May 12, 1965. The mutual backscratch-

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* See Judge Friendly's caustic comments on the Referee's performance of his duty (R. 2359-2368) and his criticism of the New York State Court settlement system.

ing which this arrangement involves fully justifies Judge Friendly's condemnation.

The burden of proof is upon Kirby to show that under the above circumstances he is entitled to plead *res judicata*. We submit that in view of the above he is unable to sustain the required burden either as to the necessary facts or on the law. No authority has been cited that enables a non-party to an action to claim *res judicata* because an objectant not a party plaintiff has "raised" the issue in a proceeding that has become moot and furthermore any judgment in which has been enjoined for *res judicata* purposes in the federal court.

Conclusion

The Court of Appeals erred in sustaining the defense of *res judicata* as to Allan P. Kirby on the question of whether the State Court had jurisdiction to enter its judgment approving his settlement and releasing the claim against him alleged under the Securities Exchange Act of 1934. Since the district courts of the United States have "exclusive jurisdiction" over such claims, the orders and judgment of the State Court and Kirby's release pursuant thereto are void insofar as they relate to the 1950 stock transaction which is the subject of the appeal herein. Accordingly, the judgment of the Court below should be reversed.

Respectfully submitted by,

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